

Message Text

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ACTION EUR-12

INFO OCT-01 AF-06 ARA-06 IO-10 ISO-00 SEC-01 SP-02 AID-05

EB-07 NSC-05 CIEP-01 TRSE-00 SS-15 STR-04 OMB-01

CEA-01 CIAE-00 COME-00 FRB-03 INR-07 NSAE-00 USIA-06

XMB-02 OPIC-03 LAB-04 SIL-01 L-03 H-02 PA-01 PRS-01

DODE-00 /110 W

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R 291331Z AUG 75

FM AMEMBASSY LISBON

TO SECSTATE WASHDC 4011

INFO AMEMBASSY BERN

AMEMBASSY BONN

AMEMBASSY BRUSSELS

USMISSION EC BRUSSELS

AMEMBASSY COPENHAGEN

AMEMBASSY DUBLIN

AMEMBASSY HELSINKI

AMEMBASSY LONDON

AMEMBASSY LUXEMBOURG

AMEMBASSY MADRID

AMEMBASSY OSLO

AMEMBASSY PARIS

USMISSION OECD PARIS

AMEMBASSY ROME

AMEMBASSY STOCKHOLM

AMEMBASSY THE HAGUE

USMISSION NATO

AMEMBASSY VIENNA

AMCONSUL OPORTO

AMCONSUL PONTA DELGADA

AMEMBASSY BRASILIA

USMISSION GENEVA

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E.O. 11652: N/A

TAGS: ECON, EFIN, PFOR, PO

SUBJECT: GOP ATTEMPTS TO SHORE UP INVESTOR CONFIDENCE

SUMMARY: IN ATTEMPT TO COUNTERACT LACK OF INVESTOR CONFIDENCE AND GROWING RUMORS, GOP HAS APPROVED FOREIGN INVESTMENT CODE, ANNOUNCED REOPENING OF STOCK EXCHANGE (BUT ONLY AS A BOND MARKET), SET UP GROUP TO STUDY PROTECTION OF SMALL INVESTMENTS IN MUTUAL AND REAL ESTATE FUNDS, AND ATTEMPTED TO REASSURE BANK DEPOSITORS. HOWEVER, MEASURES THEMSELVES WERE QUALIFIED. INVESTMENT CODE HAS WEAKENED GUARANTEES AND STRESSES PENALTIES FOR VIOLATIONS. NEW BOND MARKET NOT LIKELY TO REASSURE OLD STOCKHOLDERS, ESPECIALLY SINCE GOP NULLIFIED ALL STOCK TRANSFERS SINCE EXCHANGE CLOSURE. BANK DEPOSITORS TOLD THAT INTEREST TO BE TAXED. LIQUIDITY AND CREDIBILITY OF WHOLE BANKING SYSTEM PLACED IN DOUBT DUE TO BIG DROP IN COMMERCIAL BANK DEPOSITS AND BANK OF PORTUGAL ASSETS BECOMING INCREASINGLY PAPER ONES. END SUMMARY.

1. IN RECENT DAYS GOP HAS APPROVED NUMBER OF FINANCIAL MEASURES AND ISSUED REASSURANCES, IN OBVIOUS ATTEMPT TO COUNTERACT COMPLETE LACK OF INVESTOR CONFIDENCE AND RAMPANT RUMORS.

PRINCIPAL ACTIONS:

2. FOREIGN INVESTMENT CODE.

A. MEASURE HAS BEEN APPROVED BUT FULL TEXT NOT YET AVAILABLE. AUGUST 20 COUNCIL OF MINISTERS COMMUNIQUE SAID CODE DESIGNED TO CONTROL DIRECT FOREIGN INVESTMENT, ASSURING IT ADEQUATE PROTECTION BUT SUBORDINATING IT TO NATIONAL DEVELOPMENT. PRINCIPAL FEATURES INCLUDE NON-DISCRIMINATION, TAX INCENTIVES, AND GUARANTEES ON ACCESS TO CREDIT, TRANSFER OF PROFITS, REEXPORT OF CAPITAL, ACCESS TO STOCK MARKET, AND RIGHT TO INDEMNIZATION IN CASE OF EXPROPRIATION OR NATIONALIZATION. VITAL BUT COMPLEX SUBJECT OF TECHNOLOGY TRANSFERS TO BE TREATED LATER.

B. AUGUST 23 "EXPRESSO" OUTLINED WHAT IT CLAIMED TO BE OTHER HIGH POINTS. ACCORDING TO PAPER, GUARANTEES QUALIFIED BY REQUIREMENT FOR SIX MONTHS NOTICE OF LIQUIDATION, AND PROVISION FOR "TEMPORARY" SUSPENSION OF TRANSFERS IN CASE OF "PERILOUS" BALANCE OF PAYMENTS DEFICITS OR IF TRANSFERS WOULD CAUSE GRAVE LIMITED OFFICIAL USE

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ECONOMIC AND FINANCIAL "PERTURBATIONS". NEW FOREIGN INVESTMENT NOT ALLOWED IN DEFENSE, PUBLIC SERVICES, MONETARY AND FINANCIAL, INSURANCE, AND ADVERTISING SECTORS, OR OTHERS ALREADY NATIONALIZED "OR OF PUBLIC INTEREST", BUT EXISTING INVESTMENTS NOT AFFECTED. VIOLATIONS OF CODE, SUCH AS FALSE TRANSFER PRICING, CAN CAUSE LOSS OF ALL INCENTIVES AND BENEFITS. CODE TO BE ADMINISTERED THROUGH INSTITUTO DE INVESTIMENTO ESTRANGEIRO, TO BE SET UP WITHIN SIX MONTHS UNDER MINISTRY

OF PLANNING. FURTHER DETAILS WILL BE FORWARDED WHEN TEXT AVAILABLE.

3. STOCKS AND BONDS.

A. LISBON STOCK EXCHANGE HAS BEEN CLOSED SINCE APRIL 29, 1974. LAST WEEK GOP DECREED NULL AND VOID ALL STOCK TRANSFERS MADE SINCE CLOSURE. IN AUGUST 20 COMMUNIQUE COUNCIL OF MINISTERS APPROVED SEPTEMBER 15 RE-OPENING OF STOCK EXCHANGE, HANGE, BUT QUEC FORM OF OFFICIAL BOND MARKET. EXCHANGE WILL BE USED FOR LAUNCHING OF AND TRANSACTIONS IN BONDS WHICH ARE "MANIFESTED" IN NATIONAL INTEREST, ISSUED BY STATE, OTHER AUTHORITIES, AND COMPANIES. IN AUGUST 27 PRESS CONFERENCE FINANCE MINISTER JOSE FRAGOSO SAID THAT NATIONALIZATION OF MOST COMPANIES FORMERLY LISTED ON EXCHANGE HAD ELIMINATED NEED FOR REGULAR STOCK EXCHANGE. DURING INITIAL PERIOD, IN ORDER TO PROTECT SMALL INVESTORS, ACCESS TO MARKET TO BE SUBJECT TO UNSPECIFIED "SPECIAL CONDITIONS".

B. FIRST MAJOR TEST OF NEW MARKET EVIDENTLY TO BE FIVE MILLION CONTOS (\$200 MILLION) BOND ISSUE PREVIOUSLY ANNOUNCED (LISBON 4553 NOTAL). ACCORDING TO FRAGOSO, BOND ISSUE DESIGNED TO COVER BULK OF ANTICIPATED COSTS OF ANGOLAN REFUGEE PROGRAMS. PRESENT ESTIMATE IS THAT ANGOLAN AIRLIFT WILL COST \$80 MILLION AND ASSISTANCE (INCLUDING UNEMPLOYMENT BENEFITS) MORE THAN \$160 MILLION.

4. INVESTMENT FUNDS. IN WAKE OF WIDESPREAD COMPLAINTS FROM SMALL INVESTORS, COUNCIL OF MINISTERS ON AUGUST 20 SET UP GROUP TO DECIDE WITHIN 30 DAYS ON PROTECTION OF SMALL SAVINGS INVESTED IN MUTUAL FUNDS AND REAL ESTATE PROMOTION SCHEMES (SUCH AS TORRALTA). COUNCIL COMMUNIQUE PARTICULARLY STRESSED IMPORTANCE OF EMIGRANT SAVINGS, PAINSTAKINGLY ACCUMULATED AND "PATRIOTICALLY" SENT TO PORTUGAL, AND LIMITED OFFICIAL USE

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ALLUDED TO COMPLEXITY OF INVESTMENTS STRONGLY "PENETRATED" BY INTERNATIONAL AND DOMESTIC CAPITALISM, AND INVOLVED IN SPECULATIVE STOCKS.

5. BANK DEPOSITS.

A. BESIDES ANNOUNCEMENT OF RESTRUCTURING OF COMMERCIAL BANKING SYSTEM (NOTABLY REDUCTION FROM 22 BANKS TO 12), AND NEW STATUTES FOR BANK OF PORTUGAL (SEPTTEL), IN LIGHT OF

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ACTION EUR-12

INFO OCT-01 AF-06 ARA-06 IO-10 ISO-00 SEC-01 SP-02 AID-05

EB-07 NSC-05 CIEP-01 TRSE-00 SS-15 STR-04 OMB-01

CEA-01 CIAE-00 COME-00 FRB-03 INR-07 NSAE-00 USIA-06

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INFO AMEMBASSY BERN

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WIDESPREAD AND GROWING RUMORS GOP HAS FELT CONSTRAINED TO
ISSUE TWO STATEMENTS IN SLIGHTLY MORE THAN TWO WEEKS AFFIRMING
SOLVENCY OF BANKS AND SECURITY OF DEPOSITS.

B. AUGUST 11 MINISTRY OF FINANCE COMMUNIQUE ASSURED DEPOSITORS
THAT GOP GUARANTEES ALL BANK OBLIGATIONS. IT SAID THAT
DEPOSITS IN NATIONALIZED BANKS "ABSOLUTELY SECURE" IN
MANNER THAT PRIVATE BANKS COULD NEVER EFFECTIVELY ASSURE, AND THAT
GOP HAD ALREADY INTERVENED IN SOME BANKS WHOSE SOLVENCY HAD
BEEN THREATENED BY PREVIOUS CAPITALIST MANAGEMENT. MINISTRY
ALSO ASSURED DEPOSITORS THAT DEPOSITS NOT SUBJECT TO TAX.

C. IN AUGUST 26 COMMUNIQUE COUNCIL OF MINISTERS AVERRED THAT
SECRECY AND BANK ETHICS WILL BE ASSURED. IT HEDGED ON FINANCE
MINISTRY'S STATEMENT BY ADMITTING THAT WHILE GOP DOES NOT INTEND

TAX DEPOSITS OR DEPOSITORS, IT DOES PLAN TO TAX INTEREST.
COUNCIL ALSO CATEGORICALLY DENIED ANY INTENTION TO INSTITUTE
COMPULSORY INVESTMENT, E.G., OBLIGATORY TRANSFER OF BANK
DEPOSITS INTO SAVINGS BONDS.

6. COMMENT:

A. RAPIDLY GROWING LACK OF CONFIDENCE ON PART OF BOTH DOMESTIC
AND FOREIGN INVESTORS, WHICH IN SOME CASES IS BORDERING ON
PANIC, IS HARDLY LIKELY TO CALMED BY THESE GOP ACTIONS.
THEY EMANATE FROM A GOVERNMENT WHOSE OWN FUTURE IS FAR FROM ASSURED,
AND WHICH BESIDES IS NOTED FOR ITS SUDDEN AND RADICAL SHIFTS IN
POLICY. THEY ALSO COME IN THE SAME PERIOD THAT THE GOP HAS JUST
ANNOUNCED APPROVAL OF A DECREE LEGALLY GIVING THE WORKERS "CONTROL"
OF PRODUCTION, WHICH PLACES MEANINGFUL CONTROL OF INVESTMENT BY
INVESTOR IN DOUBT. THERE IS ALSO NO REASON TO SUPPOSE THAT GOP
WILL BE ANY MORE WILLING THAN IT HAS IN THE PAST TO IMPLEMENT
MEASURES THAT MEET DETERMINED OPPOSITION FROM RADICAL WORKERS
AND GROUPS.

B. REASSURANCES TO BANK DEPOSITORS HAVE BEEN ISSUED AMIDST
GROWING DOUBTS ABOUT, LIQUIDITY AND MAYBE EVEN SOLVENCY, OF SYSTEM.
ACCORDING TO OFFICIAL FIGURES, TOTAL ASSETS OF COMMERCIAL BANKING
SYSTEM DROPPED \$941 MILLION (7 PCT) IN 15 MONTHS FROM END OF
1973 THROUGH FIRST QUARTER OF 1975. WHILE TIME DEPOSITS ROSE BY
\$625 MILLION (14 PCT), DEMAND DEPOSITS FELL VERY SHARPLY--BY
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\$1.37 BILLION (27 PCT), AND TOTAL DEPOSITS BY \$1.05 BILLION
(11 PCT). BANK SOURCES TOLD US THAT BULK OF LOST DEPOSITS WAS
PUT "UNDER MATTRESS", ALTHOUGH SOME MAY HAVE GONE TO GOVERNMENT
SAVINGS BANK CAIXA GERAL DE DEPOSITOS WHOSE TOTAL DEPOSITS IN
SAME PERIOD ROSE \$705 MILLION (38 PCT). MEANWHILE, AT LEAST TWO
OF THREE FOREIGN BANKS HERE EXPERIENCING SURGE IN NEW DEPOSITS,
PRESUMABLY TAKEN FROM NATIONALIZED BANKS. RUMORS ABOUT BANK

LIQUIDITY PROBABLY HAVE STRONG BASIS. GOP HAS BEEN TAPPING BANKS FOR PROBABLY UNREDEEMABLE LOANS TO KEEP MANY HUNDREDS OF COMPANIES AFLOAT AS IF FUNDS WERE LIMITLESS. RELIABLE BANKING SOURCES HAVE TOLD US THAT AT LEAST ONE MAJOR BANK, BANCO PORTUGUES DO ATLANTICO, IS HAVING DIFFICULTY MEETING SALARIES FROM ITS OWN RESOURCES. HOWEVER, FIVE-FOLD INCREASE IN PORTFOLIO OF COMMERCIAL PAPER HELD BY BANK OF IRTURA

FROM END OF 1973 THROUGH MAY 22, 1975 (FROM \$450 MILLION TO \$2.27 BILLION), AND 65 PCT RISE (TO \$3.17 BILLION) IN CURRENCY CIRCULATED DURING SAME PERIOD, MAY HAVE HELPED "PAPER OVER" SITUATION, AT LEAST FOR MOMENT.

C. BESIDES SITUATION MENTIONED ABOVE, INTERNATIONALIZATION

IN BANK OF PORTUGAL NOT LIKELY TO BE HELPED BY ITS DELAYED ADMISSION IN AUGUST 23 COMMUNIQUE THAT IT HAS CHANGED ITS RULES OF GOLD COVERAGE FOR CURRENCY AND FIXED LIMITS OF CONCESSION OF CREDIT TO GOVERNMENT. (CURRENCY COVERAGE WAS 50 PCT; THE NEW COVERAGE WAS NOT SPECIFIED). BANK CLAIMED THAT THE RULES ARE NO LONGER FOLLOWED IN WORLD BANKING SYSTEMS AND WERE MERELY "DEFENSE MECHANISM" FOR FORMER CORPORATION STRUCTURE OF BANK.
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